No. 14,692

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant,

vs.

NATIONAL WHOLESALERS, a corporation, M-D PARTS MANUFACTURING COMPANY, NATIONAL PARTS COMPANY and HENRY MEZORI,

Appellees.

APPELLEES' PETITION FOR REHEARING.

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TABLE OF AUTHORITIES CITED

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APPELLEES' PETITION FOR REHEARING.

Pursuant to Rule 23, the appellees, defendants in the lower court, petition this Honorable Court, the Honorable James Alger Fee, the Honorable Richard H. Chambers, Circuit Judges, and the Honorable Roger T. Foley, District Judge, to grant a rehearing of the decision of this Court rendered September 18, 1956, reversing the judgment of the District Court made in favor of the defendant appellees, and reported in 126 Fed. Supp. 357.

The Grounds Upon Which Petitioners Seek a Rehearing.

1. The decision is in direct conflict with two recent cases decided by this Court, *Lindsay v. U. S.* (C. A. 9, 1950), 181 F. 2d 582, and *United States v. Looney* (C. A. 9, 1955), 226 F. 2d 144, which followed the rule laid down by *United States v. Moorman* (1950), 338 U. S. 457, 70 S. Ct. 288. The *Lindsay* and *Looney* cases are not mentioned in this Court's opinion herein.

2. The courts have no power to review or to set aside the decision of the Secretary of the Army or his duly authorized representative, in this case the contracting officer for the Secretary of the Army, made pursuant to Armed Services Procurement Act of 1947, Public Law 413, 80th Congress, Title 41 U. S. C. Sections 151-161, unless fraud or mistake so gross as to imply bad faith upon the part of the contracting officer enters into his decision.

3. The courts have no power to review or to set aside the decision of a department head or his duly authorized representative, in this case the contracting officer for the Secretary of the Army, made pursuant to the standard dispute clause incorporated in the contract in suit, unless fraud or mistake so gross as to imply bad faith on the part of the contracting officer enters into his decision.

4. The Government cannot maintain any sort of action to override the decision of a duly authorized contracting officer for the Secretary of the Army made pursuant to Armed Services Procurement Act of 1947 or pursuant to the standard dispute clause contained in all contracts for Army supplies without alleging and proving fraud on the part of the contracting officer or mistake on his part

so gross as to imply that bad faith entered into his decision.

5. The courts have no power to revise a contract made by a contracting officer for Army Ordnance who has been duly authorized by the Secretary of the Army to make the contract pursuant to the authority granted by Armed Services Procurement Act of 1947, 41 U. S. C. Sections 151-161.

6. The contracting officer for Army Ordnance, duly authorized to do so by the Secretary of the Army, had authority to modify the contract so as to qualify as "or equals" the regulators already delivered when the dispute arose and to direct the completion of the contract by the delivery of the same type, kind and labeled regulator.

7. The regulator generator assembly delivered to Army Ordnance by the contractor, appellee National Wholesalers, was not a proprietary article belonging to the Delco-Remy Division of General Motors, and this Court's holding as a matter of law that it was such a proprietary article added an additional requirement to the contract which was not included therein.

8. The finding of the District Court on substantial evidence that the defendant appellees committed no fraud of any sort in the transaction precludes the holding that defendant appellees did, as a matter of law, file false claims against the Government within the meaning of the False Claims Statute.

9. The uncertainties in the contract for the regulator generator assemblies on the form prepared by Army Ordnance should be interpreted against the Government.

10. Fraudulent intent of the contractor is an essential element to a recovery by the Government of the penalties prescribed under the False Claims Statute.

ARGUMENT.

I.

Without Alleging and Proving Fraud or Such Gross Mistake as to Imply Fraud Upon the Part of the Secretary of the Army or His Duly Authorized Representative Entering Into a Decision, the Government Is Not at Liberty to Attack Judicially or Administratively a Decision of a Duly Authorized Contracting Officer Made Pursuant to the Authority Granted in Armed Services Procurement Act of 1947, 41 U. S. C. Sections 151-161.

This Court says on page 9 of its opinion that there is some strength in the argument that, when the contracting officer qualified the regulator as an "or equal," he made a determination of fact binding upon the Government. This Court, however, was of the opinion that the letter of October 16, 1950, was not such a decision and says that, if the contractor's decision was such a determination, the law of the Ninth Circuit is against the defendants, citing *United States v. Lundstrom* (C. A. 9, 1943), 139 F. 2d 792. It is important to note here that the *Lundstrom* case was decided four years prior to the adoption by The Congress of Armed Services Procurement Act of 1947, Title 41, U. S. C., Sections 151-161 (S. R. 286), under which the contract for the 6600 voltage regulators was made, April 1, 1950.

The *Lundstrom* case was an action by the contractor for the reasonable value of its services performed under a Government contract. The Court says that the *Lundstrom* case is somewhat weakened by *United States v. Moorman* (1950), 338 U. S. 457, 70 S. Ct. 288. In the *Moorman* case the Supreme Court held that the decision of a contracting officer on the question of whether or not work had

been done outside of the requirements of the contract was a dispute which, when settled by the contracting officer under the standard dispute clause, could not be questioned in the courts.

We contend here that the tests of the regulator made by the Detroit Arsenal and the decision made by the contracting officer based upon those tests was a decision of questions of fact. In any event, the things decided here were certainly more nearly questions of fact than the determination of whether or not certain work, as in the *Moorman* case, was within the requirements of the contract, which would appear to be more of a question of law than the dispute involved here as to whether or not the 6600 regulators furnished to Ordnance by the contractor were inferior and failed to comply with contract specifications.

It is interesting to note how other Circuits have treated the *Moorman* case. One of the late cases from another Circuit is *Wildermuth v. U. S.* (C. A. 7, 1952), 195 F. 2d 18, where the Court, after considering the law on subjects analogous to the ones here presented and citing cases which take us over a period of more than 75 years, held:

> "However, if we are to give significance to the Moorman case, it appears inescapable that whatever doubt may have lingered in prior Supreme Court decisions, all questions are banished by the clear-cut terms of Moorman. It stands unequivocally for the proposition that today, if not before, parties to a government contract can validly provide that all disputes, whether they be of law or fact, be decided by one of their group, and that such a decision is, by the terms of this contract, 'final and conclusive.' "

Two recent cases decided by this Court, which are not mentioned in the opinion, are *Lindsay v. U. S.* (C. A. 9, 1950), 181 F. 2d 582, and *United States v. Looney* (C. A. 9, 1955), 226 F. 2d 144. The *Lindsay* and *Looney* cases follow the doctrine of the *Moorman* case and in our view reveal the error of this Court in holding that the contracting officer's determination could be ignored, without the Government pleading and proving fraud or some overreaching on the part of the contracting officer in making the decision declaring the 6600 regulator generator assemblies furnished Ordnance under the contract fitted exactly the specifications set out in the contract.

The *Lindsay* case, in which it was held that the *Moorman* case was controlling, was based on facts analogous to those of the *Lundstrom* case. This Court said in the *Lindsay* case that the District Court was right in confining the evidence to the question of the contracting officer's fraud or gross mistake on his part implying bad faith. The decision of the contracting officer was made under the standard dispute clause in that contract.

The *Lundstrom* and the *Looney* cases were both brought under the Tucker Act. The facts in both cases are quite similar. The decisions cannot be reconciled. The decisions appear to be opposites of each other. In the *Looney* case it was held that the Government and the contractor had agreed that "the contracting officer should have final say in the interpretation of the specifications." The contracting officer decided the dispute in favor of the Government and against the contractor. The District Court overturned the contracting officer's decision. This Court reversed the District Court, citing the *Moorman* and other cases to sustain its decision and held that the decision of the contracting officer on the interpretation of the specifica-

tions was final and bound the contractor. Nothing more was done here by Army Ordnance than to interpret the specifications by determining from the tests made that the 6600 regulators fitted like a glove the specifications in the contract of April 1, 1950, contained in the item description on page 295 of the supplemental record.

The *Moorman* case was said by this Court to be controlling authority for the Court's holding in the *Looney* case, as the Supreme Court had analyzed a similar dispute over the "interpretation" of a contract and held the contracting officer's decision, absent fraud or gross mistake implying fraud, to be final and not within the reach of the courts.

The *Lindsay* and the *Looney* cases are not only in accord with the decisions of the Supreme Court but those decisions are also in line with the decisions of the other Circuits among which there seems to be no conflict. An interesting case is *National Labor Relations Board v. Volney Felt Mills, Inc.* (C. A. 6, 1954), 210 F. 2d 559, citing *United States v. Wunderlich,* 342 U. S. 98, 72 S. Ct. 154, and *United States v. Moorman,* 338 U. S. 457, 70 S. Ct. 288, to the point that fraud will not be inferred and in the absence of fraud of the Government officer making the decision and in the absence of such gross mistake on his part as would necessarily imply bad faith or failure to exercise an honest judgment, a government contract committing final decision to an administrative officer with the right of appeal to the head of an agency, may not be set aside or repudiated.

This Court recognizes the above principle as stated in the *Volney Mills* case but indicates that the test of the regulator generator assembly as well as the decision of the contracting officer were limited in scope and not well rea-

soned or determinative of the dispute presented to the contracting officer. We respectfully contend that this was an erroneous approach by the Court. The authorities here cited and the new Armed Services Procurement Act of 1947, 41 U. S. C., Sections 151-161, under which the contract was made, remove from the courts the authority to overthrow a contracting officer's decision, unless fraud or gross mistake enters into his decision. (*Sunroc Refrigeration Co. v. U. S.* (U. S. D. C. Pa., 1953), 104 Fed. Supp. 131.)

We do not believe that sufficient consideration was given by the Government to the Armed Services Procurement Act of 1947 when it brought this suit. The Government, with the apparent design of escaping the certainty of a dismissal of the complaint on motion, omitted all reference to the test of the regulator and to the decision of the contracting officer. The Government must have known that the test of the regulator, made by Detroit Arsenal and the decision of the contracting officer pursuant to the authority granted him by Section 156(a) of 41 U. S. C., was final under the provisions of subdivision (c) of Section 156. Under this congressional grant of authority the contracting officer had the power to make, or to modify, or otherwise to change the contract in his discretion, and that discretion is not subject to judicial review. (*United States v. Binghampton Construction Company* (1954), 347 U. S. 171, 177, 74 S. Ct. 438, 441, and *De Cambra v. Rogers* (1903), 189 U. S. 119, 23 S. Ct. 519, 521.)

On the question, that the contracting officer's decision and the test made by Ordnance may have fallen short of what might have been required by a court in similar circumstances, a good statement is found in the case of *National Labor Relations Board v. Air Associates, Inc.* (C. A. 2, 1941), 121 F. 2d 586, 591, citing eight decisions of the Supreme Court to support the holding of the Second Circuit in that case, that the Supreme Court has during a period of more than thirty years found it both an impractical and an unwise judicial undertaking to probe the mental processes of officials engaged in reaching decisions pursuant to statute on the face of the evidence presented to them. Statutory authority for the contracting officer's decision made in the present case is found in Armed Services Procurement Act of 1947, 41 U. S. C. Sections 151-161.

This Court says that the contracting officer's decision qualifying the regulator as an "or equal" may be questioned because the procedural requirements of the contract (S. R. 292) were not observed by the contractor or the contracting officer. We contended in our briefs that this procedural requirement could, in the discretion of the contracting officer, be waived. It was held in *Service v. John Foster Dulles, Secretary of State* (U. S. C. A. D. C. (June 14, 1956), 235 F. 2d 215), that the discharge by the Secretary of State of a State Department employee under authority granted the Secretary by statute cannot be questioned in the courts, although the Secretary failed to follow the procedural requirements of an executive order of the President.

II.

The Regulator Generator Assembly Was Not a Proprietary Item.

This Court seems to have founded its reversal of the judgment upon its opinion that the contract required the contractor to furnish the proprietary Delco-Remy regulator and nothing else. The record shows that the regulator was not a proprietary item. Webster's Unabridged Dictionary defines a proprietary item as:

> "One who has exclusive title to and in; one who possesses the dominion, or ownership, of a thing in his own right; a proprietor; owner. A body of proprietors; property owners collectively. Right of property; ownership; proprietorship. Made and marketed by a person or persons having the exclusive right to manufacture and sell, such as a proprietor."

If the regulator had been a proprietary item, Army Ordnance would not have had the right to submit bids on such a proprietary article to 56 approved bidders and to receive and consider 21 bids for the 6600 regulators (S. R. 285). The contract was awarded to the lowest bidder, appellee National Wholesalers. Reference is here had to the lower court's opinion, made a part of its findings of fact [R. 52] and reported in 126 Fed. Supp. 357. In its opinion the District Court considered the Government's claim of fraud in the invoices and showed how there could be no fraud arising out of the labeling. The lower court further found in effect in Finding IX [R. 51] that the regulator was not a proprietary article but was owned by Army Ordnance which could buy it from any person who was able to furnish it. That finding is sustained by the call for bids from 56 dealers and the processing of 21 bids received. The call for bids

from 56 firms and the processing of the 21 bids received is conclusive evidence that the Government considered that it owned the proprietary rights to the regulator. At least the Government is bound by its acts so made with full knowledge of what its rights of ownership of the regulator were. Whatever uncertainties which were thus created or which appear in the contract must be construed against the Government. (Opinion of the District Court, Dec. 1, 1954, 126 Fed. Supp. 357; *Reconstruction Finance Corp. v. Sullivan Mining Co.* (C. A. 9, March 5, 1956), 230 F. 2d 247, 250.)

III.

Furnishing of Inferior War Material Which Does Not Measure Up to the Specifications Provided in the Contract Does Not Authorize an Action for Recovery of the Penalties or Damages Provided in the False Claims Statute.

The contracting officer, who, we contend, had the sole right of decision herein, held that, if the regulator were found from the test to be inferior, the Government would have the right to cancel the contract. The contracting officer said in effect in his written decision that the furnishing of a regulator of the contractor's manufacture would have entitled the Government to cancel the contract, if it had been found from the test that the regulator did not measure up to Ordnance print numbers (Ord. 7069022, Ord. 7069023 and Ordnance Stock No. 2580-118502) which was Ordnance's designation on its prints describing the regulator otherwise known as DR-1118502, GM-118502, IHC-50301-R-1. If it had been determined by the Government test that the regulator was inferior to the one contracted for under the Ordnance print and stock numbers, the Government would have cancelled the contract

and recovered the damages it had suffered. There was nothing more the Government could do. The Government had the right to terminate the contract (Par. 24, S. R. 289) whenever it suited its convenience to do so. The making of inferior war material which fails to measure up to the standard provided by a Government contract does not authorize an action for recovery of the penalties or damages provided in Section 231, 31 U. S. C. *(Hillgrove v. Wright Aeronautical Corp.* (C. A. 6, 1945), 146 F. 2d 621, 622, and *United States v. U. S. Cartridge Co.* (E. D. Mo. 1950), 95 Fed. Supp. 394, affd. (C. A. 8, 1952), 198 F. 2d 456, cert. den. (1953), 345 U. S. 910, 73 S. Ct. 645.)

It was known to the trade and to the 56 approved bidders to whom the 6600 regulators were submitted for bids that the numbers under the item description in the contract (S. R. 295) were all descriptive of the same article, and that the regulator was owned by Ordnance, and designated under its print Nos. 7069022 and 7069023 and its stock No. 2580-118502. It will be observed that the Government's complaint for recovery of the $2,000 as a penalty on each of the invoices presented is based solely upon the allegation that the voltage regulator was inferior to the one contracted for. Whether or not the voltage regulator was inferior was purely a question of fact resolved in the contractor's favor by the contracting officer for Ordnance under the dispute clause contained in the contract. The decisions of *Moorman* and *Wunderlich, supra,* and the decisions of this Court in *Lindsay v. U. S.* and *United States v. Looney, supra,* are controlling on the point that no case has or can be made against the defendant appellees without alleging and proving fraud or gross mistake of the Government's contracting officer entering into his decision.

IV.

Fraud Is a Question of Fact, Not a Matter of Law. Fraud Is Never Presumed; It Must Be Specifically Alleged and Clearly Proved.

The Government's complaint by-passes the only sort of fraud which can be urged in a case of this sort. The Government must have known when it filed the complaint that there was no way to make a case against the defendants under the False Claims Statute without first getting the tests and the decision of the contracting officer out of the way. The Government came in the back door to allege fraud of the contractor in furnishing an inferior article to the Government, which the contractor was alleged to have mislabeled in order to cover up from Ordnance the inferior character of the 6600 regulators. The tests and the decision of the contracting officer for the Government were not mentioned in the complaint. The District Court found pursuant to the agreed issues in the pretrial stipulation that the contractor committed no fraud of any kind. [Findings VI, VII, VIII and IX, R. 50-51].

In the pretrial stipulation it is said at page 36 of the Record:

> "Facts to Litigated
>
> I.
>
> "Whether the defendants conspired to defraud the United States, and to present false claims.
>
> II.
>
> "Whether the defendants knowingly and *with intent to deceive the United States* delivered regulators not in conformity with the contract, and, in so doing placed on such regulators a Delco-Remy name plate, imprint, and scroll." (Italics ours).

After the pretrial stipulation was filed the District Court held certain pretrial proceedings and at the trial took

testimony aggregating some 258 pages on the question of fraud and found on this evidence that there was no fraud as alleged in the complaint [Finding VII, R. 50], and that no false claims had been made by the defendant appellees.

The question of intent on the part of appellees to file false claims, which is discussed at some length in the opinion, seems to be unnecessary in view of the District Court's finding that there was no fraud. If there was no fraud, naturally there could be no intent to commit fraud. It is believed that this Court's decision holding as a matter of law that there was fraud herein is in conflict with the recent decisions of this Court in *Carr v. Yokohama Specie Bank, Ltd.* (C. A. 9, 1952), 200 F. 2d 251, 254-255, and *Paramount Pest Control Service v. Brewer* (C. A. 9, 1949), 177 F. 2d 564, 567, and also in conflict with the decisions of the Supreme Court in *United States v. Chemical Foundation, Inc.* (1926), 272 U. S. 1, 14, 47 S. Ct. 1, 6, and *United States v. Wunderlich, supra,* and *United States v. Colorado Anthracite Co.* (1912), 225 U. S. 219, 226, 32 S. Ct. 617, 620.

The alleged fraud pled in the complaint that the contractor furnished an inferior item not called for by the contract is all immaterial. In September, 1950, at the time that Ordnance ordered delivery of the regulators stopped until tests were made, Ordnance referred the whole matter to the United States District Attorney at Los Angeles. The then District Attorney had the F.B.I. make a complete investigation of the contractor and the methods used in furnishing the regulators [R. 255-262]. Pursuant to that investigation and the tests made, the decision of the contracting officer was rendered directing the contractor to deliver the balance of the regulators, which was done. There is no other assumption possible

than that the District Attorney at the time, September 1950, considered that there was no cause of action under the False Claims Statute. No more was heard of the subject until nearly three years later when the complaint was filed on July 3, 1953, charging the defendants with fraud in the invoices for the regulators delivered after the contractor's decision as well as those which went before.

The only kind of fraud which could have been pled and proved and which the decisions of the Supreme Court and of the Circuits including the Ninth, recognize as being material to a case of this kind is that of the contracting officer making the decision, or such gross mistake on his part as would necessarily imply bad faith or failure to exercise an honest judgment. (*United States v. Moorman; United States v. Wunderlich; Lindsay v. U. S.* and *Looney v. U. S., supra*). As said before, the decision of the contracting officer was by-passed by the Government which brought the suit in order to reach the matter in a way which has been condemned by the Supreme Court of the United States from the time of *Kihlberg v. U. S.*, 97 U. S. 398, 402, 24 L. Ed. 1106, decided in 1878, 78 years ago.

Petitioners respectfully request that a rehearing be granted.

Wm. H. Neblett,

Attorney for Appellees, Petitioners Herein.

I, Wm. H. Neblett, attorney for the appellees, petitioners herein, certify that in my judgment the foregoing petition for rehearing is well founded and that it is not interposed for delay.

Wm. H. Neblett.